



Corporate Governance scandals: Waste Management

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Overview

- **What is Waste Management?**
- **What did Waste Management commit?**
- **What was missing/what should have they done?**
- **How to fix the problem?**
- **Literature**

What is Waste Management?

Waste Management



What do they do?

- Waste Management provides collection, transfer, recycling, and disposal services to public and residential areas.



Location?

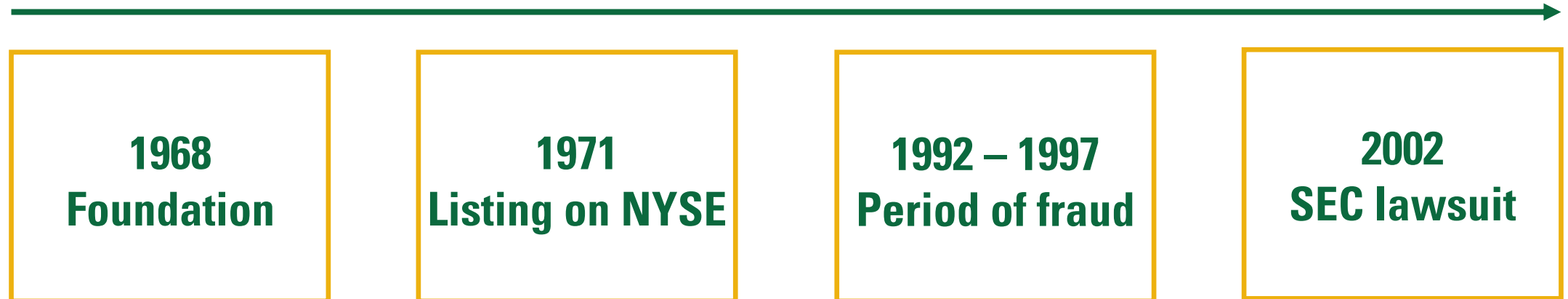
- Waste Management started in Chicago, Illinois in 1968. Now, Waste Management serves North America. Specifically, USA, Mexico, and Canada. Their headquarters is in Houston, Texas.

Who?

- Dean Buntrock: Founder and Chairman of Board of Directors of WM
- Phillip Rooney: the President and CEO
- James Koenig: the Executive Vice President and CFO
- Thomas Hau: the Vice President and CAO
- Herbert Getz: Senior Vice President and General Counsel
- Bruce Tobecksen: the Vice President of Financial Department

Background

- 1970s: Acquisitions, public listing, period of rapid growth
- 1980s: Reaching \$2 billion in revenues, departure of co-founder Wayne Huizenga
- 1990s: Cooking the books, financial reports restated for 1992 - 1997
- 2000s: The Securities and Exchange Commission investigation and lawsuit



What did Waste Management commit?

What did Waste Management do?

In short, WM conducted profit manipulation in its various forms, such as:

Avoided depreciation costs

Assigned salvage values to assets that previously had no salvage value

Failed to report expenses of decreases in the value of landfills

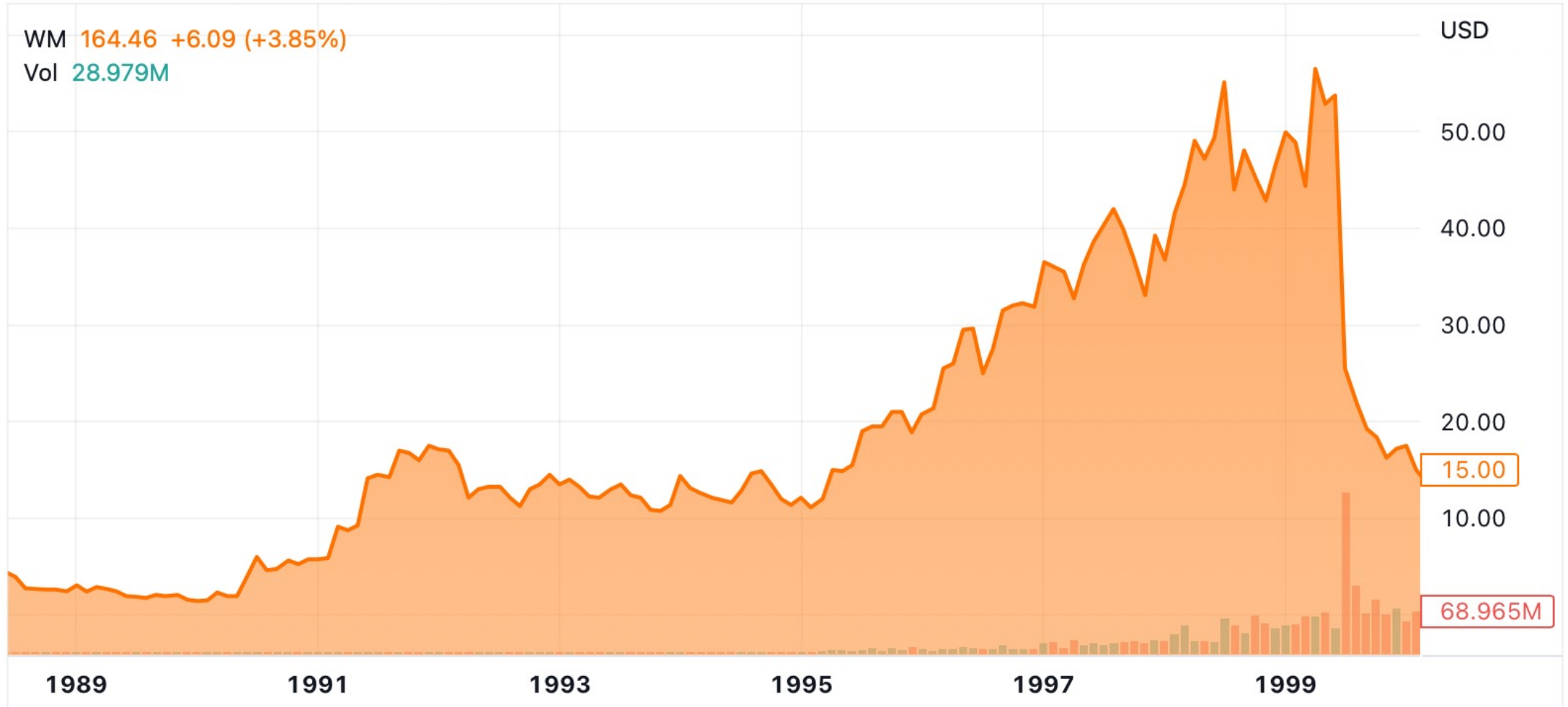
Ignored costs related to abandoned landfill development projects

Improperly capitalized a variety of expenses

Failed to establish sufficient reserves to meet its tax and other liabilities

Stock performance

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What were the gains?

Larger (disclosed) profits

Year	Originally reported (thousands)	As restated (thousands)	Amount overstated (thousands)
1992	\$ 850 036,00	\$ 739 686,00	\$ 110 350,00
1993	\$ 452 776,00	\$ 288 707,00	\$ 164 069,00
1994	\$ 784 381,00	\$ 627 508,00	\$ 156 873,00
1995	\$ 603 899,00	\$ 340 097,00	\$ 263 802,00
1996	\$ 192 085,00	\$ -39 307,00	\$ 231 392,00
Q1 - Q3 1997	\$ 417 600,00	\$ 236 700,00	\$ 180 900,00

Source: The SEC Complaint No. 02C 2180

Personal gains

	Ill-gotten gains
Buntrock (the CEO)	\$ 16 917 761,00
Rooney (the president & COO)	\$ 9 286 124,00
Koenig (the executive VP & CFO)	\$ 951 005,00
Hau (the VP & CAO)	\$ 640 100,00
Getz (Senior VP & General Counsel)	\$ 472 500,00
Tobecksen (the VP of Financial Department)	\$ 403 779,00

Source: The SEC Complaint No. 02C 2180

What led to the fraudulent accounting?



Stakeholder's expectations (pressure)

- In his interview after the scandal broke out, Buntrock claimed that in addition to company's shareholders, the market in general as well as employees expected the growth to continue



Top executive's personal traits (rationalization)

- The SEC stated that key motivators for misstating its financial figures were greed and a desire to preserve professional and social status



The role of Arthur Andersen (opportunity)

- Arthur Andersen, the external auditor of Waste Management, knew that Waste Management were understating its costs and thereby, by its own actions, enabled Waste Management to falsify financial reports

What was missing/what should have they done?

THE FRAUD TRIANGLE



Source: Cressey, 1953

Opportunity:

Opportunity refers to circumstances that allow fraud to occur. In the fraud triangle, it is the only component that a company exercises complete control over. Examples that provide opportunities for committing fraud include:

- Weak internal controls
- Poor tone-at-the-top
- Inadequate accounting policies

Pressure:

Pressure refers to an employee's mindset towards committing fraud. Examples of things that provide incentives for committing fraud include:

- Bonuses based on a financial metric
- Investor and analyst expectations
- Personal incentives

Rationalization:

Rationalization refers to an individual's justification for committing fraud. Examples of common rationalizations that fraud committers use include:

- "Others are doing it as well"
- "There is no other solution"



Dean Buntrock, BoD Chairman of WM
Driver behind the fraud

Opportunity:

- Dean Buntrock is the Founder and Chairman of the Board of Directors of WM
- The precursor of WM is a small waste business in Colorado owned by the Huizenga, Buntrock's ex-wife's family. Buntrock and his team led WM expansion across America
- Executives like Rooney (the President) was scouted by Buntrock and was groomed to become his successor
- Other Executives (Koenig – the CFO, Hau – the CAO, Tobecksen – Vice President of Finance) came from Arthur Andersen, the auditor of WM
- Lack of ethics from the auditor – Arthur Andersen: received additional fees outside auditing agreements to issue unqualified opinions on WM's financial reports
- Lack of ethics in WM's culture: the Executives were known to be controlling and did not allow others to question their actions; Buntrock persuaded other Executives to join his scheme: aggressive accounting culture

Pressure:

- WM started to exit the fast-growing state and entered more mature, stable state
- Failing to meet the predetermined targets (set by Buntrock) and expectations of analysts for more growth
- Buntrock's income were tied to WM's stocks
- Earnings from stock price increases were used to purchase other companies to further accelerate growth
- Keeping the good image as the pillar of the community: the founder of several local trade organizations and recipients of various Awards like the Horatio Alger Award and the inductee of the Sales & Marketing Executives International Academy of Achievement
- Even in 1997, 1 year before the fraud got exposed, Buntrock was named outstanding chief executive in the pollution control industry by Financial World and The Wall Street Transcript

Rationalization:

- Since the fraud was conducted for 5 years (1992-1997), he might have thought that he would not be caught
- Other Executives also agreed to conduct fraudulent actions alongside him (in fact people love to hire those who share their value system)
- Buntrock was a philanthropist and had been a generous benefactor for numerous institutions, he might consider increasing his wealth to help the unfortunate was a right thing to do (the end justifies the mean)





Phillip Rooney



Thomas Hau

Other Executives:

Phillip Rooney: ensured that required write-offs were not recorded and overruled accounting decisions that would have a negative impact on operations

James Koenig: ordered the destruction of damaging evidence, misled the Company's audit committee and internal accountants, and withheld information from the outside auditors

Thomas Hau: acted as Koenig's sous-chef for cooking the books

Herbert Getz: blessed the Company's fraudulent disclosures

Bruce Tobecksen: handled Hau's overflow

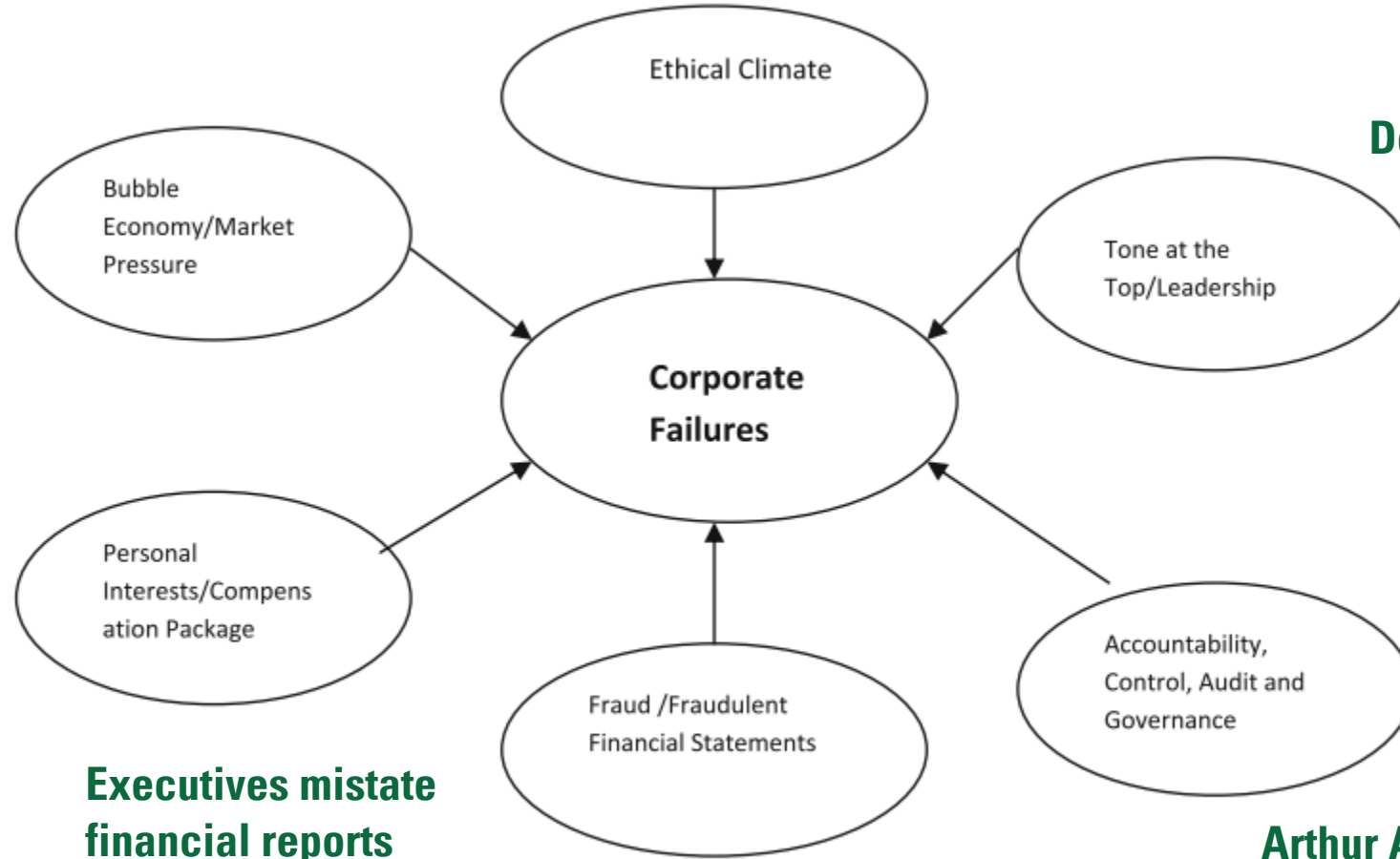
The Differential Association Theory (Sutherland, 1947)

- Most of the learning of criminal behavior happens within close, personal groups rather than from detached communications.
- The learning of criminal behavior also includes the learning of techniques used to commit crime as well as the motives and rationalizations that are associated with crime.

Unethical, fraudulent actions conducted in groups

Decreasing growth

Stock-based compensation



Dean Buntrock

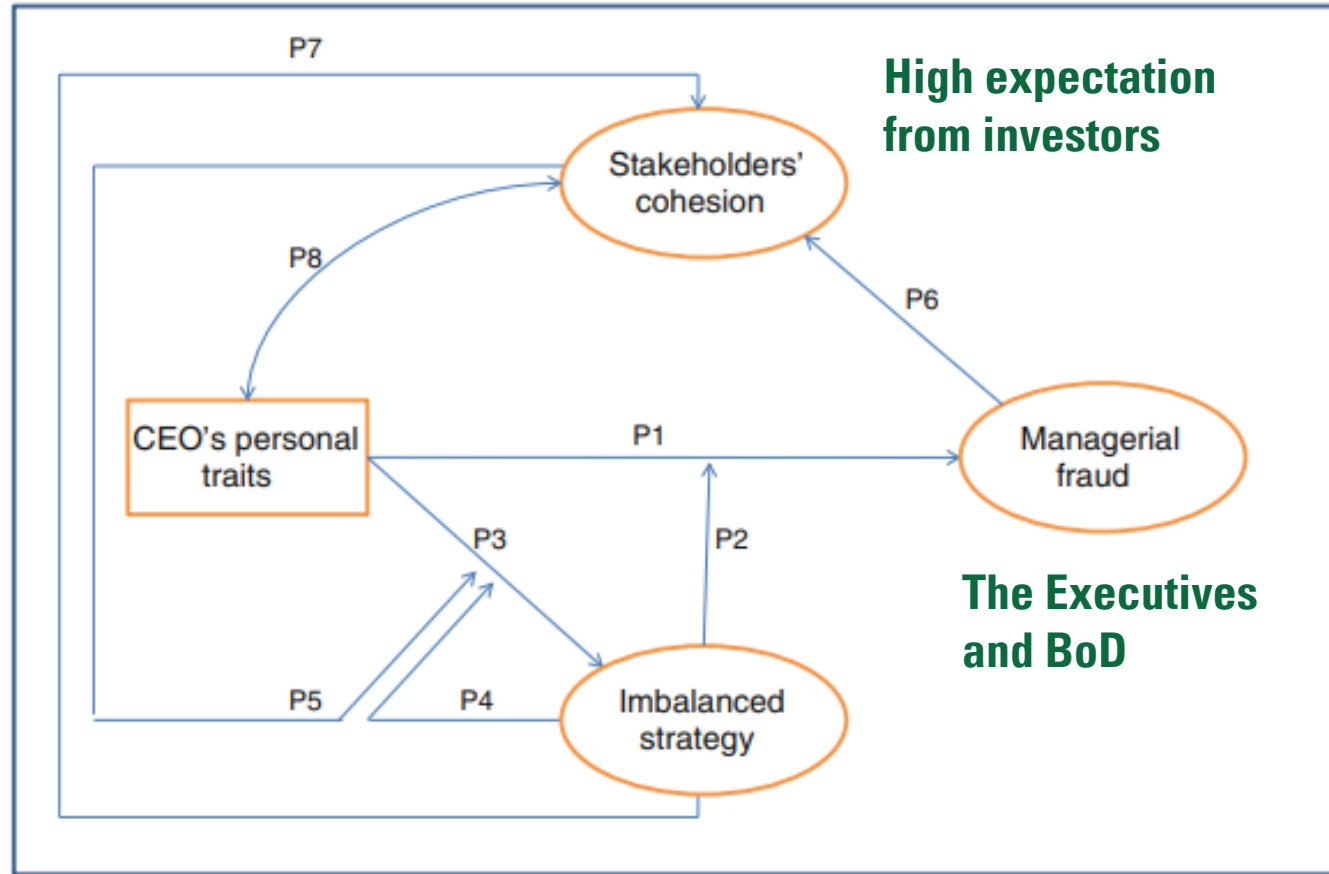
Executives mistate financial reports

Arthur Andersen

Theoretical framework indicating the possible major causes of corporate failures

Source: Zona et al. (2013)

Dean Buntrock



The antecedents of corporate scandals

**Aiming for great growth when
the business entered the
mature state**

Corporate
scandals

What should they have done?

- Hire a new CEO
- Hire a different auditor that did not have such a cozy relationship to the officers of WM
- In order to eliminate the opportunity factor of fraud, other officers such as the CFO and CAO that have more direct influence on the financial statements of the company would have had to be replaced

How to fix the problem?

Actions taken after the fraud

- **Replacement of the CEO and auditor**

- **Multiple CEO's during 1996-2004**

- **Acquired by USA Waste Services in 1998**

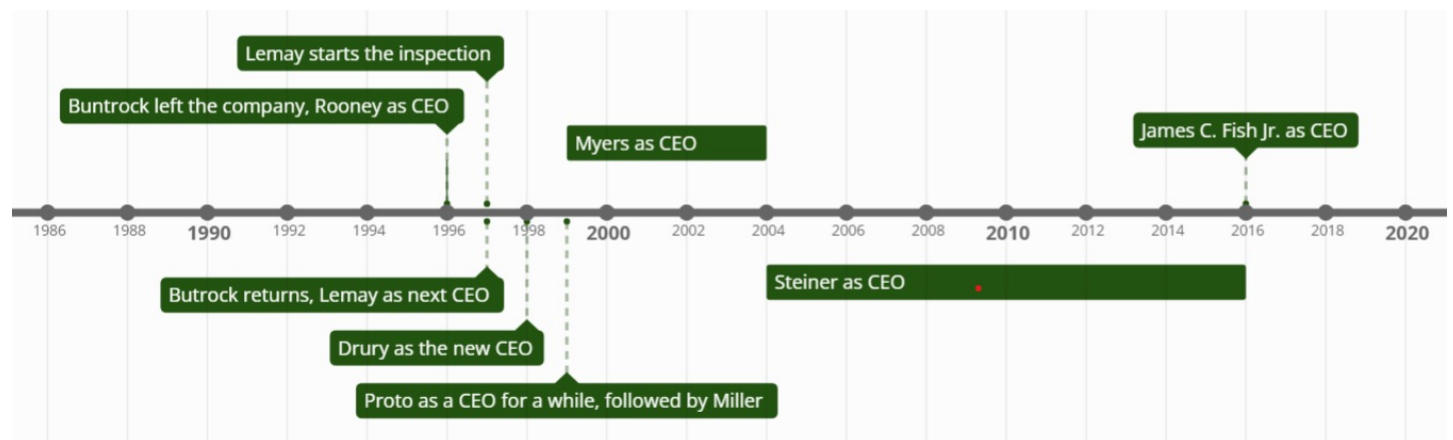
- **USA Waste Service's CEO**
- **New outside Chair for Board**

- **External auditor Arthur Andersen replaced**

- **Financial restatements for 1992-1997**

- **\$1,7 billion worth of pre-tax earnings**

- **Actual profitability enabled survival**



Aftermath

- **Suspension, civil cases filed and ban from public companies as directors for people in charge of the fraud.**
- **\$26,8 million settlement cost for Waste Management, \$31 million fines for the managers.**
 - **\$457 million liability for shareholders.**
- **\$7 million settlement cost and significant reputational damage for Arthur Andersen.**
 - **Consequences for participation were not efficient.**
- **Sarbanes-Oxley Act 2002.**
- **Rebranding to WM in 2022.**
 - **More focus on sustainability, new technologies and operational practices.**

What to learn from this?

- **Family relations and other dependencies can potentially be enablers of immoral actions.**
 - **Financial restatements are more likely when a founding member is the CEO, less likely when the Chair of Audit Committee is independent.**
- **External revisors better off as completely independent.**
- **Regulations and laws are necessary for ensuring quality of auditing.**

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